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RUEHLO/AMEMBASSY LONDON 8092
RUEHKP/AMCONSUL KARACHI 9886
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UNCLAS SECTION 01 OF 02 ISLAMABAD 002108

SENSITIVE
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E.O. 12958: N/A
TAGS: ECON EFIN ETRD EAGR ENRG PREL PGOV PK
SUBJECT: PAKISTAN'S 2008-09 BUDGET: NO MONEY SLOTTED FOR ENERGY
INFRASTRUCTURE UPGRADES, PART TWO OF THREE

¶1. (SBU) Summary: On June 10, Finance Minister Naveed Qamar delivered the Government of Pakistan's (GOP) proposed budget for fiscal year 2008-2009 which must still be approved by the National Assembly. Despite acknowledging that the shortage of energy and prolonged nationwide blackouts were the worst in Pakistan's history, the Finance Minister did not propose any budget allocations for energy infrastructure upgrades or new construction. He acknowledged that the GOP is paying USD 554 million per month for current subsidies on petroleum and will attempt to reduce these subsidies in the coming fiscal year. Calling for increased private investment, Qamar unveiled a proposed budget which fell short of addressing the nation's current energy crisis. Other proposed energy incentives include the duty free import of energy efficient light bulbs and generators. End Summary.

SUBSIDIES: WORSE THAN PREVIOUSLY DISCLOSED
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¶2. (U) The 2007-2008 federal budget provided 114 billion rupees (USD 1.68 billion), accounting for 1.1 percent of total GDP, for subsidies which were split among petroleum, electricity, wheat, textiles and fertilizers. However as world prices increased, the subsidies swelled out of control and became unsustainable resulting in a ballooning federal deficit. Qamar acknowledged that the total expenditures on these subsidies in the 2007-2008 fiscal year totaled 407.5 billion rupees (USD 5.99 billion), accounting for 3.9 percent of total GDP, with the bulk spent on petroleum at Rs. 175 billion (USD 2.59 billion); electricity Rs. 133 billion (USD 1.97 billion); wheat Rs. 40 billion (USD 591 million), and textiles and fertilizers Rs. 48 billion (USD 709.5 million). For petroleum alone, Qamar disclosed that the GOP paid Rs 37.5 billion per month (USD 554.4 million), or Rs 1.25 billion per day (USD 18.48 million).

¶3. (U) Qamar stated that the new budget proposes to reduce the volume of total subsidies by 27.5 percent to Rs 295 billion (USD 4.4 billion) to account for only 2.4 percent of GDP. He specifically cited three subsidies for energy providers. First, a Rs 74.612 billion (USD 1.1 billion) subsidy is planned for the Water and Power Development Authority (WAPDA) to compensate for the varying tariffs rates applied by the distribution companies operating in different regions of the country. A special provincial allocation of 12.5 percent is provided for Balochistan to ensure the continued function of electricity providers and the agricultural irrigation "tubewells." Qamar noted that in the 2007-08 budget, the government

had estimated Rs 52.893 billion (USD 781.9 million) for this purpose, which was increased to Rs 113.658 billion (USD 1.68 billion). Second, a continued but reduced subsidy for Pakistan's largest power provider, the Karachi Electric Supply Corporation (KESC) from Rs 19.6 billion (USD 289.7 million) in 2007-2008 to Rs 13.8 billion (USD 203.9 million) for 2008-09. Third, a reduced Rs 140 billion (USD 2.1 billion) allocation, compared to Rs 175 billion (USD 2.59 billion) in 2007-08, to pay subsidies to the oil marketing companies.

PRIVATE SECTOR INVESTMENT TO THE RESCUE?
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¶4. (U) Qamar called upon the private sector, "both from indigenous sources as well as from outside," to increase investment in key infrastructure projects. He scolded the previous government for not supporting the rising growth rates with infrastructure upgrades in either the public or private sectors. Qamar noted that Pakistan is currently facing the most severe energy shortages and blackouts in its history with a peak demand-supply gap recorded at 4500 mega watts. He also stated that increased exploration for natural gas is necessary to bridge the rising demand-supply gap of nearly 1.5 bcf and noted that this gap must be addressed through "imports and cross border pipelines." Calling the current independent power providers (IPPs) "our saviors," Qamar implied mistreatment by the previous government towards the IPPs stating they "were unjustifiably maligned and castigated." However, the proposed budget falls short of providing incentives or promoting measures to attract private sector investors in the energy field.

ENERGY SAVING INCENTIVES
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¶5. (U) As part of the budget speech, Qamar also highlighted several measures aimed at addressing the current energy crisis in Pakistan. All energy saver lamps will be exempted from sales tax in order to promote their use. The GOP optimistically states that this incentive will save 1000 mega-watts of electricity. Further "Energy Saving Incentives" include the elimination of customs import duties on energy saver light bulbs, generators, and "deep cycle batteries" which are exclusively used in solar energy equipment. The GOP also proposed a temporary duty reduction, from five percent to zero, on the importation of power generation plants for the Water and Power Distribution Authority (WAPDA) and the generation companies (GENCOs).

COMMENT
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¶6. (SBU) The proposed 2008-2009 GOP budget fails to address the serious energy crisis currently facing Pakistan. Upcoming debate in the National Assembly will likely not provide any noticeable increased in energy budgets. While the proposed subsidies for energy in the 2008-2009 budget reflect significant reductions, they have not yet been substantiated with either increased prices at the pump for consumers or increased electricity charges. Such shocks will certainly be met with rage and disdain among average Pakistanis who cannot afford the current subsidized prices. Cabinet level meetings have reportedly discussed phasing out the petroleum subsidies by the end of the current calendar year which is simply not feasible given that the current world price of USD 132 per barrel and the price currently passed onto the Pakistani public is approximately USD 76 per barrel. GOP continues to falter in its energy planning and has failed to address the critical energy shortfall threat facing the nation in this proposed budget. End Comment.

PATTERSON